UNITED
NATIONS

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Economic and Social Council

Distr.
GENERAL

E/1991/82
12 June 1991

ORIGINAL: ENGLISH

Second regular session of 1991
Geneva, 3-26 July 1991

# IMPACT OF THE RECENT EVOLUTION OF EAST-WEST RELATIONS ON THE GROWTH OF THE WORLD ECONOMY, IN PARTICULAR ON THE ECONOMIC GROWTH AND DEVELOPMENT OF THE DEVELOPING COUNTRIES, AS WELL AS ON INTERNATIONAL ECONOMIC COOPERATION

Report of the Secretary-General

SUMMARY

As a contribution to the deliberations of the special high-level meeting of the Economic and Social Council called for in General Assembly resolution 45/182, Council resolution 1990/68 and Council decision 1990/205, the present report examines the impact of the recent evolution in East-West relations on the growth of the world economy, in particular on the economic growth and development of the developing countries, as well as on international economic cooperation.

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## INTRODUCTION

1. Changes in East-West 1/ relations in recent years have been momentous, but they continue to evolve as the process of transition in Eastern Europe and the Soviet Union is proving to be more painful and protracted than anticipated. The outcome of this complex political restructuring is not yet in sight, and the positions taken towards it in the rest of the world are as yet tentative. The implications for the world system remain in many respects speculative. This is especially true about the impact of the changes in East-West relations on the world economy in general, and on developing countries in particular. As has been said so often, there is no historical precedent for the processes under way in the East. The following analysis seeks only to bring together the most salient features of the issue, to identify the uncertainties and, to the extent possible, to point to policy options.

### The economic situation in the East 2/

2. Considerable progress in market-oriented reforms has been achieved in the biggest countries in Eastern Europe, but the Soviet Union and Yugoslavia are facing growing economic problems, and overall there was a fall of over 6 per cent in output and incomes in 1990. This was one of the reasons why the rate of growth of the world economy was 1 per cent, two percentage points below that in 1989. However, as a result of the relatively autarkic nature of the past regime of central planning, the economic impact of the contraction in the East on the world economy is relatively limited and is concentrated in neighbouring European countries and in the small number of developing countries in which, for political reasons, Eastern trade and aid was of significant proportions.

3. One of the principal reasons why the reforms in the East have proved so difficult has been political disagreement about a new and market-oriented dispensation. In some cases, this has been complicated by ethnic and regional conflict. But events that were not anticipated in early 1990 have greatly aggravated the situation, notably: (a) the disintegration of the traditional trade and payments arrangements among the countries of the East in the Council for Mutual Economic Assistance (CMEA); 3/ (b) the unification of Germany and the disappearance of the German Democratic Republic 4/ from the regional economic organization of the East; (c) the recession in the Organisation for Economic Cooperation and Development (OECD) countries; and (d) the crisis in the Gulf.

### Trends and prospects in trade

4. The dismantling of State trading, the abandonment of the transferable rouble regime for trade in CMEA, the integration of the German Democratic Republic into the Federal Republic of Germany and the attempt to institute hard currency trading as of the beginning of 1991 have had profound consequences for the trading patterns of Eastern countries. Intraregional trade and trade with CMEA developing country members (Cuba, Mongolia and

Viet Nam) is contracting rapidly. Hungary and Poland had already begun to increase their exports to OECD countries before 1989. Vis-à-vis developing countries, there is a switch from former political allies to other developing countries, especially the newly industrializing countries of Asia. Those developing countries that had significant trade relations with the CMEA countries, such as India, may encounter difficulties in adjusting to the sudden changes in the trade patterns of these countries. Declining oil output in the Soviet Union has reduced its export and consequently its import capacities.

5. The Eastern share of total OECD trade was of the order of only 1-2 per cent in the 1980s. The impact of present changes is negligible except in Germany, where the sudden integration of the German Democratic Republic has posed more acute problems than in the rest of Eastern Europe. Some developing countries will face increasing competition in the markets of the OECD countries, especially after the European Community's decision to accord preferences to Eastern European countries. On the other hand, the opening up of Eastern markets offers new opportunities.

Finance and debts

6. Several of the Eastern countries (especially Bulgaria, Hungary, Poland, Romania and the Soviet Union) were able to borrow heavily in the 1970s and 1980s. Their combined debt rose from a negligible level in 1970 to $80 billion in 1980 and $153 billion in 1990. Romania was forced into debt rescheduling in 1982 and then repaid its debts by 1989 through a wrenching austerity programme. Poland declared a moratorium in 1981, Bulgaria in 1990. It is not clear how the recent relatively large Polish debt relief will affect the debt relief prospects of developing country debtors.

7. At present, commercial banks do not lend to the East and they do not see this problem as linked to lending to developing countries. Official assistance commitments to Eastern countries for 1990-1992 (excluding the European Bank for Reconstruction and Development (EBRD)) are estimated at $4.5 billion a year, about one tenth of the disbursements of official development assistance (ODA) to developing countries. Although there has been no diversion of aid funds so far, the prospect cannot be excluded.

Development assistance

8. Eastern foreign aid to developing countries was tied and provided through merchandise exports and technical assistance. It was mostly channelled to countries of ideological affinity with a commitment to industrialization in the context of a sizeable State sector. It has always been difficult to compare it with the ODA of the OECD countries, as defined by the Development Assistance Committee (DAC) of OECD. The East never subscribed to that definition. In the 1980s, the Soviet Union, Bulgaria, Czechoslovakia and the German Democratic Republic submitted reports on their foreign aid, based on their own definitions, which showed it to be at or above the target of 0.7 per cent of GDP. OECD estimates of Eastern aid according to its criteria

range between 0.14 per cent in 1975 and 0.23 per cent in 1985, but this may underestimate the value of non-conventional forms of resource transfers such as price concessions and large numbers of scholarships.

9. Eastern development assistance to political allies is now being drastically reduced or abandoned, and there is now interest in collecting debts from these countries. What will happen to the aid programme of the German Democratic Republic is unclear.

10. Another aspect of developing country cooperation was the admission of an unknown but substantial number of workers and trainees, chiefly from developing country CMEA members, to Eastern Europe and the Soviet Union.

Migration out of the East

11. Before 1989, only Hungary and Yugoslavia allowed their citizens to work abroad, although there was a steady trickle of migrants from most countries in the East. Hundreds of thousands of Yugoslav migrants had moved to the OECD countries since the 1960s. But migration, especially from the German Democratic Republic, suddenly swelled in 1989 and triggered the great transformations of that year.

Problems encountered in economic reform

12. As well as being an end in itself, a more vibrant democracy may be necessary to make the adjustment burdens of the transition socially acceptable. However, greater public dissension makes it more difficult for Governments to provide the firm leadership that is called for in moving from political to economic management. The unsettled state of political issues in the Soviet Union bears heavily on the economic prospects of the region as a whole. There is in all countries, in varying degrees, a lack of legal institutions and financial infrastructure; and privatization on the scale that is involved raises enormous problems. Until more of the uncertainty about the economics and politics of reform in the East is removed, economic stability is restored, and basic infrastructure - in telecommunications, roads, commercial banking and property rights - has been put in place, foreign investors are unlikely to take the very large risks of moving production facilities into the East on a large scale.

Changes in East-West relations

13. The first and foremost change in East-West relations has been the end of the cold war and ideological conflict, with all its implications: the resumption of cultural and intellectual contacts, the restoration of the United Nations to its original function, which was premised on East-West accord, and a halt to the arms race, which only a few years ago was a major preoccupation of the international community.

14. Only a few years ago, East and West were competing in building support for antagonistic alliances. But in 1990 the issue of Western assistance for

the transformation of the East rose to the top of the international agenda, and the Eastern countries intensified their approaches to Western organizations for economic cooperation. The past neglect of environmental issues in the East attracted great attention, both in the East itself and world wide.

15. The course of events in Germany provides a stark illustration of the consequences of a sudden opening of the borders between economies with very different real incomes. The fear that a pronounced deterioration in the socio-economic situation in other Eastern countries might stimulate a mass migration towards the West is a strong incentive for Western European countries to support development in the East.

Impact on developing countries

16. The short-run impact of the collapse of CMEA on the three developing-country members has been quite adverse. The economic strains of the East and its new policy orientation have also cut short its development assistance programmes. But concerns about the long-term impact of the new East-West relations on developing countries in general relate to (a) the risk of a significant diversion of public and private capital flows from the South to the East, accompanied by an increase in the cost of financial capital; (b) displacement of developing country exports in OECD markets by competitive manufactures and commodities from the East; (c) a general shift of attention in Governments and international organizations towards the problems of the East at the expense of the development problems of the South and (d) the rise of "political" conditionality and possible conflicts over the role of government in development. However, against these should be set the potential for gain from (a) new markets for developing countries in the East (tropical products, electronics); (b) the freeing up of resources from disarmament in the North, the South and the East; and (c) the new potential for attention to global issues, including world-wide development.

17. No firm conclusion can be drawn about the impact of all these changes on developing countries. For several, there will be unavoidable losses in the short to medium term; for most, the changes will provide new challenges as well as opportunities. So far it is impossible to claim that either positive or negative effects on developing countries in general seem probable in the foreseeable future. What will happen to flows of public capital and development assistance, which is where conflict seems most likely to occur, remains for Governments to decide.

Events in Eastern Europe and the United Nations system

18. The transition in the East has primarily engaged the attention of two groups of countries - the East and the developed market economies. However, the process has implications for all countries, including the developing countries. The United Nations has a role to play in ensuring that it is successful, by helping in the task of coordinating the different technical assistance and financial cooperation efforts and by working for the

improvement of the statistical base, which will help in the monitoring and evaluation of the evolving situation. It also has a vital role to play as a forum for enhanced global dialogue, which should help to address the matter of the possible negative effects of the transition process, especially on developing countries. All countries have a stake in the progress of the others and enhanced cooperation would help to ensure that the transformation in the East will indeed be a positive-sum game.

Policy issues

19. A great historical event has occurred - the coming, and in some cases the return - of democracy to Eastern Europe and the end of ideological confrontation between two apparently contradictory ways of organizing socio-economic life. The changes under consideration involve a move towards a universal organization of the world economy, which, as long as the economies in the East remain in a state of uneasy transition, will continue to raise difficult issues of monetary, financial and commercial cooperation. In the end, this major event is likely to enhance substantially the functioning of the world economy, as the great human and natural resources of the East are brought into play with greater efficiency, but the time that history will require for the modernization of the East with its many countries and regions cannot be readily ascertained and could probably be shortened by the appropriate responses. Among the many issues that arise a few stand out:

(a) The countries of the East are moving from a system of managed trade, based largely on transactions among themselves, to greater integration in the world economy, based upon trade conducted in convertible currencies. According them adequate access to global markets, while at the same time enhancing the access of all countries to each other's markets, will be a major issue in global trading negotiations. The East is going through a very painful transition from one system of trade to another, and thought should be given to ways to maintain the momentum of intra-trade during this period so as to ease the difficulties attending the transition process;

(b) There is a large array of efforts by international organizations to assist Eastern countries financially and in all conceivable aspects of institutional and intellectual reform. This whole issue of East-West technical cooperation, involving many different multinational and international institutions, is one that would appear to call for greater coordination. At the same time, the free flow of ideas forms the basis of the free market economy. But there is the possibility of over-kill - that the administrative abilities of the economies in transition will be overwhelmed by trying to provide the inputs for the advice being given and in absorbing and reconciling all the different advisory reports that accompany most assistance. There is perhaps a case for greater humility in assisting agencies. They should realize that this is an unprecedented situation and that they should not undervalue the degree of knowledge of policy makers of their own economies and of the precise difficulties that they face. The record of outside expert advisers in developing countries is not such as to inspire complete confidence in the success of outside advice in the case of the former centrally planned economies;

(c) If the international financial organizations are to be able to meet both the needs of the economies in transition and the developing countries, they will require capital increases. In particular, the ratification of the ninth quota review of the International Monetary Fund should be accelerated, and an early start made on the tenth quota review, especially in light of the possibility of the Soviet Union's future participation in the Fund;

(d) At least in the short- to medium-term, multilateral surveillance should pay special attention to a balanced approach regarding the source of funds for financial assistance to the transition process. A continuation of a stringent monetary policy in some of the large Western European economies at a time of increasing financial requirements would tend to perpetuate high real interest rates;

(e) The recent treatment of debt relief has raised some difficult questions as to whether the countries in the East are being given especially favourable treatment and whether many of the developing countries, particularly heavily indebted countries, deserve comparable or even better treatment. In any event, the adverse consequences of excessive debt burdens have again been given international prominence and steps have been taken to forgive the debts of countries whose policies are expected to lead to recovery in the long run. This should help the international community advance to a solution to the overall debt problem;

(f) The environmental problems of the East have been seen in their full enormity with the coming of political liberalization and greater openness. International organizations have added important programmes in response to requests from member States. If they are not undertaken in the context of the general transformation process, there is a danger that they could simply divert attention from key issues;

(g) The situation of the East has enlarged the agenda of the United Nations and its family of specialized agencies. The Organization will be hard pressed to maintain a sense of perspective and not to stretch its limited resources too thinly;

(h) There is a critical need for better statistical information of wider coverage from countries of the East. This should enhance the monitoring process and work towards the establishment of an effective early warning system. More fundamentally, it should facilitate the involvement of these countries in the different attempts at economic coordination at the global and regional levels;

(i) In the short run, the developing countries can be expected to see the attention paid to the East by the developed market economies as "special treatment" for a group of countries that have strong cultural and ethnic ties with many of the OECD countries, many of which ties are not shared by numbers of developing countries. Unless all parties see the long-term issues involved, the atmosphere for international dialogue could deteriorate. Building an international climate of confidence and trust is therefore

essential. This can be greatly facilitated if the urgent humanitarian and economic problems, such as those emerging once again in Africa, receive immediate international attention; if the deeper economic crisis in that continent is addressed with much greater commitment than has been forthcoming thus far; and if the long-standing issues of external debt, trade and finance that are holding back development in many developing countries evoke a positive response from the international community;

(j) The long-term issues involved have, to a great extent, been clarified by the end of the cold war. The countries of Eastern Europe saw that respect for human rights and greater democratization were values and rights in themselves and that their frustration had helped produce the social and economic crisis that brought about the end of one-party rule. The argument that such matters are purely domestic affairs is increasingly questioned in discussions of development issues, and gradually international cooperation is taking them into account;

(k) Finally, there is the issue of disarmament, the reduction of military expenditures and the "peace dividend". In the new international climate, substantial reductions in defence expenditures should become a realistic policy objective not only in the developed market economy and the transition countries but in developing countries as well. While, initially, reduced expenditures can cause disruptions in production and employment, eventually resources can be released for more productive socio-economic activities resulting in increased well-being.

## I. BACKDROP TO THE CORE ISSUES

Reasons for optimism: the end of the cold war

20. The recent evolution in East-West relations, often described as the end of the cold war, will have repercussions in almost all areas of international concern: global peace, disarmament, economic growth, trade, finance and international cooperation. This is because it affected not just relations between the world's two most powerful military nations, the Soviet Union and the United States of America, but also between them and third countries, including especially developing countries. The Soviet Union, and, for a long time, the Eastern European countries, did not participate in the international financial institutions, the International Monetary Fund (IMF) or the World Bank, even though several of them had attended the Bretton Woods Conference which established these bodies. Their non-participation was a clear indication that the differences were not just political differences between the Eastern European countries and the Soviet Union, on the one hand, and the developed market economies on the other, but were also ideological. They concerned views on the scope of international cooperation in economic and financial matters and the most appropriate path that the non-industrialized and poorer countries should take to achieve socio-economic development.

21. With the end of this ideological confrontation, the prospects for international cooperation at regional and international levels have been greatly enhanced. This has been seen in agreement among the five permanent members of the Security Council. The possibilities of cooperation within other bodies of the United Nations system has also been greatly enhanced and gives promise for the more effective functioning of the world body, not only in political, but also in social and economic matters. In the long term, then, it is quite likely that the recent evolution in East-West relations on the growth of the world economy, in particular on the development of the developing countries, as well as on international economic cooperation, will be positive.

22. However, to assess the short- and medium-term effects of such a change as the end of the cold war is difficult and any conclusions must be tentative. There is no historical precedent for what is taking place: the rapid change-over from one economic system, centrally planned, to another relying mainly on free markets. The changes are being attended by considerable disruptions in economic activity in all the countries of Eastern Europe and the Soviet Union, and not all the elements of the economic system that they will have at the end of the period of transition are in place or have even been agreed upon.

23. The general feeling of optimism that first attended the changes in the East has now become more subdued. This turn-around occurred quite quickly and the reasons for it will be analysed below.

The economic outlook as assessed in early 1990

24. At the start of 1990, although the short-run outlook for economic growth in the East was not very encouraging, the international community and many policy makers were optimistic regarding the prospects for medium- to long-term development of individual countries as well as the region as a whole. Some expected the latter to become a new "growth pole" for the world economy. Indeed, the political changes that had been taking place signalled a determination on the part of policy makers in the East to foster rapid changes in society's make-up and the allocation of resources. Some commentators felt strongly that the marketization and democratization of the East would unleash indigenous sources of growth that would influence favourably the global economy. Also, the end of the cold war itself would release funds for more productive investments. In this auspicious climate, multilateral and bilateral financial support - so the reasoning went - would unleash significant private initiative to mobilize capital funds, including those from abroad. In the light of these considerations, the transitions in the East were welcomed by many former adversaries in the international community as deserving quick and extensive support.

25. At that time, in early 1990, the leadership of the Soviet Union had not yet committed its prestige to the creation of a market economy; even elementary steps towards political pluralism were not yet in place. None the less, major changes in the role of the Communist Party in the economy and

society and a sense of optimism as to what would soon happen intimated that beneficial effects from credible reforms could be anticipated. Certainly, questions were raised regarding the scale of effort required for restructuring the Soviet economy and whether economic assistance from the developed market economies could possibly rival that already committed to the rest of the East. Even so, it was hardly doubted that "proper" reform policies in the Soviet Union would elicit a sizeable transfer of resources.

Concern over the effects on developing countries

26. Simultaneously, some voices in the international community raised concerns about the negative effects for developing countries of the ongoing transformation of the East. They felt it would in the short run reduce the demand for imports from those developing countries where such demand had previously been justified on non-economic grounds; it would in particular divert capital flows from and complicate the process of obtaining technology by developing countries; and it would raise trade competition for developing countries, especially in Western Europe but also in Asia. Also, the transition would elicit a demand for capital goods and technology for which many developing countries could not (yet) hope to compete.

27. It was also widely feared that the East would obtain preferential access to markets, especially in Western Europe. Moreover, the volumes of official financial assistance being earmarked by the West to ease the transition could encroach on development assistance otherwise appropriated for developing countries by the official multilateral institutions, in the event of their capital resources not being raised, as well as by national Governments, whose budgets have recently been under severe pressure. Furthermore, the attractiveness of the East for portfolio and foreign direct investment was deemed to jeopardize the flow of private finance into developing countries. Finally, it was felt that any facilities extended to accommodate labour migration, especially into Western Europe, would threaten the livelihood of existing migrant workers and exert downward pressure on the stream of remittances so vital to the foreign-exchange earnings of some developing countries.

Reasons for expectations not being realized

28. In this event, few of these fears have so far been justified. Some are unlikely to materialize soon, if at all, given the nature and pace of the transition in the East. Considerable progress towards market reforms has been made in the economies of Eastern Europe, but in the Soviet Union there is still no definite strategy concerning political pluralism and a market-oriented system, and the concepts advocated by different groups are often vague, contradictory and sometimes simply populistic. In the Soviet Union, and also Yugoslavia, ethnic rivalries are aggravating an already tense situation.

29. Yet even in those countries where the firm political decision was taken to base economic decisions henceforth on market criteria and to open up the

economy, stability and sustainable growth did not automatically result. In fact, the socio-economic situation in most of the East deteriorated rapidly, even in cases when sizeable resources from the outside could be mustered.

30. Developments that were unforeseen in early 1990 proved critically important; four stand out. First, in early 1990 it could not be assumed that the traditional trade and payment arrangements within the context of CMEA would abruptly cease to exist. Second, the existence of the German Democratic Republic as a separate economic and political entity had not yet been seriously called into question. Third, economic activity in the West slowed down. Fourth, the crisis arose in the Persian Gulf. The latter two developments affected the availability of resources for development assistance and the buoyancy of international trade.

The economic situation in the East

31. The outlook for regaining stability throughout the area is uncertain. The pace of the reform process is not wholly clear. Progress with reform in countries such as Czechoslovakia, Hungary and Poland slowed down in late 1990 because of inaction on the institutional front and political disagreements. The reform in Czechoslovakia was initiated only in early 1991 in the form of shock therapy. Bold, if partial, measures were taken in early 1991 in Bulgaria and Romania. In the Soviet Union, the outlook for genuine reforms is uncertain. In a number of cases, ethnic strife, regional and ethnic conflicts and contentious debates over sovereignty are considerably hampering the reform effort.

32. External-payment balances have deteriorated rapidly, owing to adverse terms-of-trade developments and export-revenue losses. The external payments crisis has a number of causes. Perhaps the most critical was the switch-over at the beginning of 1991, at least in principle, from the traditional transferable-rouble 5/ trade and payment regimes in CMEA to convertible-currency settlements and trading at current world prices (or emulations thereof). In addition, the collapse of CMEA, without there being a substitute arrangement, has led to re-bilateralization of trade and payments agreements, which in turn has compounded the difficulties in policy-making. The sudden renunciation of previously concluded long-term specialization and trade contracts and the sharp deterioration in the terms of trade of fuel importers on account of the crisis in the Middle East, albeit transitory, have aggravated the problem.

33. The external payments picture suggests that the future will see a protracted period of austerity, with sharply reduced levels of accumulation. The East is unable to divert trade to the West without incurring marked terms-of-trade and/or export-revenue losses. Policy makers in the area are very sceptical about the merits of regional economic cooperation among themselves. They hope that sufficient financial assistance from abroad will be forthcoming. Yet this is unlikely to be sufficient to sustain high levels of economic activity, and so there may be a sharp cut-back in aggregate demand in the group. This could have debilitating consequences for the reform movement and stability in the area. It could also constitute, for the

immediate future, a drag on the world economy. The latest estimates are that there was a fall in output and income in 1990 of 6 per cent, which is one reason why the rate of growth of the world economy was only 1 per cent, two percentage points below that in 1989.

## II. TRADE AND PROSPECTS IN TRADE

### The economic weight of Eastern Europe and the Soviet Union

34. The impact of the economic decline in the East on the global economy is, however, relatively limited. One reason for this is that the countries of Eastern Europe and the Soviet Union are considerably smaller players in the world economy than their population size or strategic and political importance would imply. The size of the population of the Soviet Union in 1991 was estimated at nearly 291 million, and that of Eastern Europe (excluding the population of the former German Democratic Republic), at 97 million, 6/ constituting respectively 5.4 and 1.8 per cent of the world's total.

35. Until recently, it was estimated that the GNP of the Soviet Union was about one half that of the United States of America, 7/ but this was revised downwards to about one third. 8/ More recent estimates by the International Monetary Fund are that the Soviet Union's GNP is of the order of 4 per cent of world GNP, and that of Eastern Europe (excluding the former German Democratic Republic) is 1.6 per cent - a combined total of 5.6 per cent. 9/ This would make the Soviet Union's GNP significantly less than a third of that of the United States. These figures imply that Eastern Europe's GNP is close to the world average, and that the Soviet Union's is about three fourths. In terms of income, these countries are closer to the levels of the developing countries rather than those of developed countries. As a group, they are about the same economic weight as Latin America, which accounted for 5.7 per cent of world GNP.

36. For the sake of comparison, Germany (again excluding the former German Democratic Republic), with 1.1 per cent of the world's population, has 6.6 per cent of world GNP, greater than the Soviet Union and Eastern Europe combined.

37. Because of the autarkic nature of the past regime of central planning, the Eastern countries had rather limited trading relationships with countries other than each other and a limited number of developing countries for which political considerations largely determined trading patterns. The contribution of the Soviet Union to total world exports of goods and services was estimated at 3.6 per cent and that of Eastern Europe at 2.2 per cent, a total of 5.8 per cent, which was again smaller than that of the unified Germany, with a total of 13.6 per cent of world exports.

### Past trading patterns of Eastern Europe and the Soviet Union

38. To a considerable extent, the future change in trading patterns in Eastern Europe should be seen as a reversion to normal trading patterns.

After the Second World War, Eastern Europe was cut off from its traditional markets in Western Europe and had to shift the bulk of its trade to the Soviet Union in a very short period of time. This artificially created trade pattern largely reduced the benefits from specialization and contributed to the ultimate dismantling of CMEA.

39. Overall, Eastern Europe's exports were concentrated in manufactured goods and the Soviet Union's in fuels, raw materials and semi-manufactured products. Arms were a large percentage of total exports - according to one source, in 1988 they amounted to nearly 10 per cent of the total exports of the Warsaw Treaty Organization countries, and almost 20 per cent of those of the Soviet Union. 10/ Trade in agricultural products and durable consumer goods occupied a comparatively small share (20-30 per cent for exports and 25-30 per cent of imports) of these countries. The share of manufactured consumer goods remained low, at about one tenth of exports and imports.

40. Data on trade volumes point to a secular decline in real growth, except in the case of Soviet imports and Polish exports, and perhaps also Romanian exports. With the exception of the Soviet Union, both export and import intensities declined sharply. Real exports to market economies contracted sharply in the second half of the 1980s. The share of Eastern Europe in the imports of the OECD countries was slightly over 1 per cent, and falling. An indication of the past failure of the Eastern countries to penetrate developed market economy markets - and of the present potential for them and other countries, if they are able to produce goods of a sufficiently high quality - is that the newly industrializing countries increased their share in OECD imports from 4.2 to 9 per cent between 1970 and 1984.

41. Intragroup trade was a large percentage of total trade. In the 1980s it amounted to about half of overall trade, 11/ when data are converted at official exchange rates, and around one third, when converted at more meaningful cross-rates between the transferable rouble and the dollar. Most countries made a major effort to bolster intragroup trade, particularly during the first half of the 1980s. Moreover, this share tended to rise after the mid-1980s basically because of adverse terms-of-trade effects, notably for total exports of the Soviet Union (largely due to falling oil prices) and total imports of Eastern Europe.

42. At the same time, trade with the developed market economies lost importance. The share of Soviet exports that went to developed market economies, chiefly in Europe, dropped from 36 per cent in 1980 to just over 20 per cent in the late 1980s. The corresponding shares for Eastern Europe are about one fourth in the early 1980s and just over one fifth by the end of the decade. Similarly, on the import side, the share of developed market economies in Soviet imports contracted from nearly 40 per cent in the early 1980s to less than 30 per cent by the end of the decade. The corresponding share for Eastern Europe was around 30 per cent early on in the decade, and slightly more than 15 per cent towards the end.

43. The vast bulk of exports to the developed market economies consisted of fuels, industrial raw materials and foodstuffs. The East as a whole did not achieve any great success in supplying manufactures to the developed market economies, and tended to import manufactures from other sources. The share of finished manufactures in their trade with the developed market economies amounted to roughly one fifth, as compared to 45-54 per cent in the case of intragroup trade and 33-44 per cent in the case of exports to developing countries. Manufactures imported from within the group took up 50-54 per cent of the total, in contrast to 29-45 per cent for developed market economies.

44. The share of non-socialist developing countries in Soviet exports rose from some 18 per cent in the mid-1970s to just under one fourth in the late 1980s. The share of trade with the former Asian planned economies doubled, in large measure because of the renewed trade ties with China. On the other hand, Eastern Europe's exports to developing countries underwent several changes, with their share dropping from 13 per cent in the early 1980s to slightly over 10 per cent by the end of the decade.

45. The developing countries did not capture a large share of the import market in the East. Their share in total Soviet imports remained comparatively small (about one sixth) and exhibited a marked decline in the second half of the 1980s. The small share of the former Asian planned economies more than doubled during the decade. The share of developing countries in Eastern Europe's imports remained at about one twelfth.

46. In sum then, trade between the East and the non-socialist developing countries has always been marginal, rather unstable, heavily concentrated on a few partners and dominated by quite traditional forms of exchange: overwhelmingly, manufactures exported by the East in exchange for foodstuffs, fuels and industrial raw materials.

The future prospects for trading relationships

47. The relevance of these past trading relationships of the East for future trade relationships depends critically on the nature of the transition, the objectives of these countries with respect to their involvement in the global economy and the concrete trade and payment regimes they will put in place. In general, the more distorted were past external linkages, as measured by real economic scarcities, and the more rapid and profound the transition to market-based decision-making, the larger will be the impact of the transformations for the rest of the world economy. These repercussions will manifest themselves directly through structural transformations in trade, which cannot but effect changes in existing markets as the reforming countries attempt to capitalize on their comparative advantages. In the future, factor endowments and productivity levels will be critical determinants of the prospective foreign demand and supply of the East.

48. The difference in levels of GNP per head between the West and the East were noted above. Relatedly, productivity levels in the East are well below half of what they are in the West. This gap stems largely from the ways in

which these countries were managed and the more general biases in resource allocation introduced during most of the post-war period. The future reallocation of resources will affect the level, commodity composition and geographical direction of trade, regardless of the trade and payment regimes, that are enacted. But the latter are important. Having taken the resolve to adopt broad, market-oriented decision-making, all reforming countries have committed themselves to reducing significantly barriers to trade that have traditionally shielded their domestic markets. Most unconventional obstacles to trade will be replaced by instruments that conform to market principles. Quantitative and other non-tariff restrictions will be considerably whittled down and the remainder mostly transformed into ad valorem tariffs. Also, these countries are revising their customs regimes, and most are bent on reducing tariffs to the sensible minimum. As foreign competition increasingly helps to streamline the allocation of resources, considerable trade creation should result, given the differences in productivity levels and the determination of policy makers in the reforming countries to close the gap as soon as is feasible.

49. To put matters in perspective, it should be noted that the population in the East, without the Soviet Union, is just under the combined total of France and the United Kingdom of Great Britain and Northern Ireland. Including the Soviet Union, it is only slightly less than that of the European members of the OECD. This suggests that if these countries succeed in narrowing the gap between their levels of factor productivity and those of the West, they could constitute a significant source of growth in the world economy for several years to come. The reintroduction of a much greater degree of consumer sovereignty cannot but produce important changes in consumer demand. For the time being, these modifications are taking place at a much reduced level of real purchasing power as compared to what consumers used to perceive as their real incomes, taking into account the very significant non-monetary transfers that traditionally occurred under central planning. None the less, once the modifications in incomes and consumer demand take shape, there should be a sizeable import demand for goods that used to be chronically in short supply in the East. This should benefit, in the first instance, imports of tropical fruits and beverages for which income elasticities, even at presently reduced income levels, are considerable. Next in line will be consumer electronics and durable consumer goods for which the elasticity of demand with respect to income is very high.

50. Upon regaining some semblance of economic stability, the reforming countries may initially capitalize on their low wage cost in international terms and could become more formidable competitors of developing countries, particularly in markets of Western Europe where they enjoy the advantage of proximity. They are bound to compete with many products at the lower end of technological sophistication, at least in the short to medium run. There are already signs of these changes. In 1990, some of the reforming countries, particularly Hungary and Poland which had already begun to increase their exports to the OECD countries before 1989, achieved impressive gains in exports to industrial countries. They even had trade surpluses with these countries at this time of wrenching changes. Their exports to the industrial

countries were not in the form of raw materials and other low processed goods, but included machinery and transport equipment.

51. Once the process of rapid marketization gets firmly under way, a major impetus to global trade is likely to materialize, which should be to the benefit of developing countries. The East needs sizeable imports of capital goods from developed countries, and the latter are likely to seek to capitalize on the relatively cheap and well-trained labour resources of the East. If successful, it would call for relatively quick changes in wage and income levels in the East, thereby creating additional room for competition on the part of the developing countries. It would also enable them to strengthen their position in the markets of many developed countries, as the competitive position of the reforming countries based on low-wage levels is likely to be rapidly replaced by skill-intensive, hence higher-cost, goods.

52. The Eastern countries themselves should become important markets for developing countries. One reason for the strengthening of the competitive position of developing countries is that the economies of the East will increasingly reflect underlying economic scarcities, many of which can be filled by developing countries. Another factor will be the abolition of the State monopoly of foreign trade and payments, which used to so much complicate access to these markets (except Yugoslavia). This was nowhere more onerous than for countries, including many of the more dynamic developing countries, that chose to eschew broad Government-to-Government trading and financing agreements with the East. In the short run, though, some considerable ingenuity, especially through trade financing, will be required to establish positions in these emerging markets of the East. This is particularly so at a time when marked structural transformations are materializing and there is little chance of quickly instituting currency convertibility.

The Eastern countries and international trading agreements

53. The reforming countries are obtaining easier access to the markets of the developed market economies. Tariffs against them are being reduced, they are being granted most-favoured nation and Generalized System of Preferences (GSP) treatment, or are being allotted larger quotas for traded goods that are "managed". Ways are being sought to bring them more closely into the framework of the European Community and the European Free Trade Association (EFTA). "European agreements" on association status with the Community are currently under negotiation with Czechoslovakia, Hungary and Poland; a commitment in principle has been made to have them in place by 1 January 1992. With the EFTA, the same three countries are also negotiating preferential free-trade agreements.

54. The question whether such enhanced access is at the expense of developing countries has been raised. The removal of discriminatory quantitative restrictions imposed on Eastern exports should be welcomed for its own sake, as well as when placed in the context of the need for greater trade liberalization. The more complete adherence of the reforming countries to the discipline of the General Agreement on Tariffs and Trade (GATT) would place

the access of reforming European countries to the markets of contracting parties under agreed disciplines for which enforcement mechanisms exist, though they have not been very effective in recent years. It should also give an impetus to buttressing GATT. It would strengthen the framework for trade expansion once the reforms in the East take off.

55. Preferential treatment accorded to the East that might result from the negotiations with the Western European partners could be considered undesirable if they could not be reconciled with article XXIV of the General Agreement. 12/ None the less, the impact of the actual and potential preferential arrangements should not be exaggerated. Current negotiating stances in the European negotiations, for example, point to reductions being enacted only for manufactures and, even then, only for those that are not short-listed as "sensitive" in some sense. That means that the bulk of the potential offer of manufactures from the East, if competitive at all, will not benefit from the discriminatory removal of the European Community's external tariffs on them.

The effects of the dissolution of CMEA

56. Another concern has been the effects of the disintegration of CMEA on its members. This has had dramatic effects on the European members. The Eastern European countries had thought that the Soviet Union would continue to be an important market for their products as they gradually became more competitive in Western markets, but, because of a shortage of hard currency and administrative changes, the Soviet Union's demand for imports from Eastern Europe declined dramatically after the beginning of 1991. The Soviet Union was particularly concerned to harness its hard currency earnings to buy equipment for its oilfields from the developed market economies, so as to prevent a decline in production there and, in turn, earn export revenues.

57. The effects of German reunification on the former German Democratic Republic probably swamp any effects that would have been felt from the dissolution of CMEA. Enterprises of the former German Democratic Republic have been left without much ability to improve their competitiveness through devaluation, as distinct from the other Eastern European enterprises, nor do they have the same degree of tariff protection that still prevails in Eastern Europe.

58. The dissolution of CMEA has also transformed the outlook for other countries. Three developing countries were full members of CMEA: Cuba, Mongolia and Viet Nam. Eight developing countries were "cooperants": 13/ Afghanistan, Angola, Ethiopia, Iraq, Mexico, Mozambique, Nicaragua, and the Democratic People's Republic of Yemen - now again Yemen. Some other developing countries maintained "close ties" with CMEA: Algeria, Cambodia, Egypt, India, Iran (Islamic Republic of), Morocco, Pakistan and Syrian Arab Republic.

59. Trade with the three developing countries that were full CMEA members remained of marginal importance to Eastern Europe proper (about 1 per cent for

both exports and imports), but not to the Soviet Union (in recent years, about 9 per cent of exports and about 7 per cent of imports). Furthermore, their share steadily increased, especially with the Soviet Union, but with the export share remaining well above the import share.

60. Though the shares of these countries in the trade of Eastern Europe and the Soviet Union remained small, that trade was critical for them. Thus, during the 1980s, the share of CMEA in the total exports of Cuba ranged between 65 and 87 per cent, in the case of Mongolia between 92 and 93.5 per cent and in that of Viet Nam between 41 and 66 per cent. The corresponding import data are 76 and 86 per cent for Cuba, 93 and 98 per cent for Mongolia and 56 and 79 per cent for Viet Nam.

61. Similar observations apply to the eight developing-country cooperants. Their share in the trade of Eastern Europe and the Soviet Union was rather unstable, fluctuating between 1 and 2.5 per cent of exports and 1 to 1.5 per cent of imports. The importance of the Eastern partners in the trade of these cooperants, though quite significant for several of the group, was much smaller than in the case of the three CMEA developing countries.

62. The group of developing countries with "close ties" with the East accounted for about 3 to 5 per cent of their exports and imports (3 to 6 per cent for the Soviet Union). Export shares tended to exceed import shares, except in recent years, but the gap was larger for Eastern Europe than for the Soviet Union, especially during the 1980s.

63. The partner countries are being affected by a diversion of trade away from them in favour of OECD partners, particularly in Western Europe. The short-term trade outlook for Cuba, Mongolia and Viet Nam, has become very precarious indeed. As political considerations lose their relevance, the other developing countries can also be expected to transfer their trade away from former political allies towards other developing countries, including the newly industrializing countries.

64. The greater commercialization of exchanges will not just change the terms of trade, but might also compress or eliminate other elements of trading relationships, such as scientific and technical cooperation. In general, trade and assistance previously conducted on the basis of political or ideological considerations will be severely pruned.

## III. FINANCE AND DEBTS

65. For the foreseeable future, Eastern Europe and the Soviet Union will be seeking financial assistance from the developed market economies directly or from the multinational financial institutions.

Debt relief

66. Much of the assistance, in terms of the amounts of finance involved, that has been given to the Eastern countries has recently been in the form of debt relief, mainly to Poland.

67. The countries of Eastern Europe and the Soviet Union were able to borrow easily on international markets in the 1970s. Estimates suggest that the gross debt of Eastern Europe (omitting the former German Democratic Republic, but including the Soviet Union) rose from $5.6 billion in 1970 to some $80 billion in 1980; after some reduction in 1983-1984, to $90 billion in 1985; and to some $153 billion in 1990. Net debt (that is, gross debt minus deposits in banks that report to the Bank for International Settlements) rose from $3.7 billion in 1970 to $65 billion in 1980, $69 billion in 1985 and $129 billion in 1990. Whereas during most of the 1970s and early 1980s the key borrowers were Hungary, Poland and Romania, in recent years a substantial proportion of the rising debt has been on account of Bulgaria, Hungary and especially the Soviet Union. The largest lenders have been France, Germany, Italy, Japan, the United Kingdom and the United States, and some oil-exporting countries of the Middle East.

68. During the global financial crisis of the 1980s, all substantial borrowers in Eastern Europe, as well as Yugoslavia, encountered external-payments constraints of various dimensions and, especially in Hungary, Poland and Romania, the after-effects of their borrowing are now a major constraint on policy flexibility.

69. Two countries, Bulgaria and Poland, declared a formal moratorium on debt-servicing. Poland did so in August 1981. Bulgaria quickly came to grips with its first external-payments crisis in the late 1970s, essentially by re-exporting oil from the Soviet Union, but policy makers lost control over external balances in the late 1980s, and in March 1990 declared a debt moratorium. Romania was forced into formal debt-rescheduling in 1982; it decided to repay all of its debt as rapidly as possible, which it accomplished by 1989 through a wrenching austerity programme.

70. In early 1990, the Paris Club tacitly allowed Poland not to service its debt and to defer all payments of interest and principal on official debt at least until March 1991. More recently, on 15 March 1991, Poland was granted relief of official debt of about 50 per cent by the Paris Club, with several countries (notably Germany and the United States) adding bilateral debt-relief measures. In May 1991, Poland informed its bank creditors that, in July 1991, it would pay $100 million worth of interest arrears on a total of $11 billion outstanding debt owed to the banks. 14/

71. The Polish example has again brought to the forefront the question of how to solve the debt problems of other countries, those in transition as well as many developing countries. If the Polish example implies a tacit recognition by its creditors that sizeable external debts do place a debilitating damper on structural-adjustment programmes, then the future possibility for coming to

grips with developing-country debt, as well as debts of countries in transition, looks slightly brighter than it did during most of the 1980s.

Balance of payments assistance

72. Whereas in late 1989, most financial assistance provided to the Eastern European countries, excluding the Soviet Union, was for emergencies, in 1990 the focus shifted to correcting chronic balance-of-payments difficulties. 15/ Because two of the reforming countries - Poland and Yugoslavia - had just declared internal convertibility for current transactions and Hungary had relaxed considerably its trade regime, the international community wished to assist these reforming countries by easing their current-account constraints.

73. Management of the bulk of the assistance has been entrusted to five regional and international organizations (IMF, the World Bank, the European Community, OECD and the European Bank for Reconstruction and Development (EBRD)). Although not all assistance is being channelled through these agencies, most is predicated on the recipient reaching an "understanding" with IMF about restoring macroeconomic balance. Not only does such an agreement lead to stand-by loans or extended credit facilities from IMF, 16/ but it is also the main trigger for disbursements by most other donors.

74. Bringing the economies in transition under IMF's current-account discipline should, in the medium to long term, be highly desirable. For one thing, the movement towards currency convertibility in the East cannot but facilitate the access of developed and developing countries to these markets. Currency convertibility, at least for current-account transactions, is not a requirement of IMF membership (as stipulated in article VIII of IMF's Articles of Agreement). However, in view of the possibility of attaining article XIV 17/ status, achieving convertibility has been allotted a high priority by the political leaderships of the East.

Assistance to the Soviet Union

75. In the matter of international assistance, the Soviet Union is different from the other Eastern European countries, largely because of the size of its economy and because the goals of its transition are still ill-defined.

76. In 1990, international economic assistance to it was prompted by the emergence of severe external financial difficulties as well as pervasive domestic supply shortages. Addressing the Soviet Union's financial problems has posed some institutional problems as it is not a member of the international financial institutions and is not likely to be admitted in the near future. The Soviet Union is a founding member of the EBRD, but its borrowing will be strictly limited to its paid-in contribution. It is not included in the initiative of the Group of Twenty-four.

77. Owing to the above considerations, most of the assistance extended in 1990-1991 has been in the form of official bilateral arrangements, as well as

voluntary contributions by humanitarian organizations. In response to requests by the Soviet authorities, several countries and the European Community offered emergency foodstuffs, medical assistance as well as other help, usually in the form of foodstuff loans. On top of this, various Governments announced some $22 billion in bilateral credits and other financial assistance (such as government guarantees) to the Soviet Union. Some of these facilities were drawn down immediately to settle payment arrears, which had risen markedly in late 1989 and early 1990. But other disbursements are being constrained by conditions placed on the type of goods or time-frame for which guarantees can be invoked.

The volume of financial assistance extended to the East

78. Precisely how much assistance has thus far been provided to support the economies in transition is not known. At the April 1991 session of the Economic Commission for Europe (ECE), a spokesperson for the European Community reported that total commitments to the Soviet Union amounted to ECU 34 billion, and to the rest of the East to ECU 30 billion (or just under $90 billion in all), but no details were provided. Another estimate is that the total of assistance from IMF, the World Bank and Governments of the developed market economies should reach $17 billion in 1991, in addition to the more than $16 billion in debt relief accorded to Poland and the amounts that Germany will provide for the former German Democratic Republic. 18/

79. The disbursements and commitments relating to the integration of the former German Democratic Republic into Germany are, indeed, a significant addition to the fiscal expenditures of the latter and will likely be needed for a longer period than foreseen before the integration process began last year. The greater demand for money and credit that economic integration entails also raised inflationary expectations and pushed up German interest rates. In February of this year, the central bank raised interest rates directly under its control to the highest levels since 1982 in order to maintain a tight anti-inflationary stance. The deutsche mark nevertheless fell 18 per cent against the dollar and 6 per cent against the yen between mid-February and early April. The German Government passed a tax increase in March (to begin in July), and forecasts of German economic growth this year and next have begun to be revised downwards, which should ease inflationary expectations. But interest rates in Germany, and in the other countries of the European Monetary System, are expected to remain high, especially when set against actual inflation.

80. Total financial commitments made to Hungary and Poland by late 1990 amounted to some $21.2 billion, of which about 59 per cent had been provided by individual Governments and the remainder by various international organizations. 19/ These are sizeable sums, but modest in comparison with the estimated transfers of $30-35 billion, solely in non-debt creating financial aid, extended by Germany to its eastern part in 1990. Furthermore, of the total commitments to Hungary and Poland, about $12.8 billion is in the form of new loans, $5.1 billion in the form of investment and credit guarantees, and the remainder, $3.3 billion, in the form of grants and technical assistance.

These sums are upper-limit commitments for which disbursement may occur over several years, chiefly between 1990 and 1993. Rather little of this amount was disbursed in 1990. The situation could change in 1991. In April of the current year, IMF approved another $2.5 billion in loans to Poland.

81. International assistance to the other countries of the East has not been as well publicized, in part because commitments have been made more recently or are still under negotiation. By far the largest were made by the international financial institutions, with Czechoslovakia obtaining some $1.8 billion from IMF in balance-of-payments support and another $1.4 billion from the European Community as a guarantee for stabilization and convertibility. Bulgaria recently obtained a possible total of over $0.6 billion from IMF. Romania is still negotiating with IMF. Once in place, these arrangements trigger commitments by the World Bank and under the PHARE (Pologne-Hongrie: Assistance à la restructuration économique) 20/ programme, amounting to several billion dollars.

82. One important kind of assistance, that has usually accompanied financial assistance, has been technical advice. Advice has ranged from the basics of banking, through how to stabilize the economies during the period of transition, all the way to macroeconomic policy formulation in a market environment with pluralistic decision-making. A substantial component of technical assistance has been earmarked for fighting pollution in the East, both in trying to overcome the legacies from the past as well as avoid taking decisions that may aggravate the already serious ecological situation.

The effect on flows of development aid

83. Thus far, assistance to the East has not necessitated sizeable increase in the budgets of donor agencies, because disbursement has been slow, many commitments have only contingent-liability implications, and much of the assistance delivered came from excess reserves of government-subsidized foodstuffs. These factors could all change and bring into question whether assistance to the East will be at the expense of aid to other countries.

84. The assistance extended by Germany to its Eastern part is, of course, different from assistance to the other economies in transition. The length of time that such assistance will be extended will depend on how soon the situation in the Eastern part can be stabilized and productivity levels raised.

85. Regarding ODA, most OECD countries are on record to the effect that they will not divert to the East funds earmarked for developing countries. Instead, funds for the East will on the whole be additional appropriations in ODA budgets. Concerning the orders of magnitude involved, assistance from the OECD countries and other official financing to Eastern Europe could average $4.5 billion per year over the next three years, which is about one tenth of total ODA from DAC.

86. It can be argued that the additional funds channelled to the East could have been allocated to developing countries. On the other hand, without the

extraordinary events in the East, there would probably not have been political support in the OECD countries for raising ODA appropriations. Since the aid budgets of several developed countries have recently come under increasing pressure, careful monitoring of the situation and coordination of the stances of all actors involved in this unprecedented cooperation process would, therefore, seem advisable.

87. As regards other financial transfers from bilateral and multilateral agencies, the reforming countries of Europe are in a potentially competitive situation vis-à-vis developing countries. In some emergency situations, substantial aid donors to the East may feel they have a small amount of room for revising upwards appropriations in their national budgets. However, the budgets of the multilateral agencies may have to be raised to maintain their potential and desirable levels of lending to developing countries, while at the same time allowing for increased appropriations for the East. Unless there is an increase in subscriptions, particularly to IMF and World Bank, available resources will have to be spread around more thinly, to the apparent disadvantage of developing countries as a group.

88. Some IMF resources have already been called upon by the indebted countries of the East. In the case of those countries that were already members of IMF - Hungary, Poland and Yugoslavia - the sums would probably exceed what would have been forthcoming in the absence of the revolutions since 1989. But these demands on IMF resources are unlikely to be such as to inhibit IMF from financing the "normal" balance-of-payments requirements of other members. However, if substantial structural-adjustment loans were to be granted, pari passu with the recent package negotiated for Bulgaria and Czechoslovakia, competition for such IMF resources might well materialize. This makes it more than desirable to achieve quick ratification of the ninth review of IMF quotas and an early start to the tenth review.

Private lending and investment inflows

89. As concerns private bank participation in new medium- and long-term sovereign, infrastructure or balance-of-payments lending, the overall policy of the banks is based upon what they consider purely commercial criteria: to avoid commitments to countries that have rescheduled and to most other developing countries. The Eastern European countries are, then, in the same position as most of the developing countries in not having access to such sources of finance.

90. From the early 1970s on, the countries of Eastern Europe and also Yugoslavia tried to attract foreign venture capital through various joint ventures laws, 21/ which were revised several times over the years, usually resulting in foreign capital being granted more liberal access. Yet, comparatively small amounts of capital came into the East prior to recent reform announcements. The number of joint ventures rose rapidly after perestroika made it possible for these activities to blossom also in the Soviet Union and after the inauguration of market-oriented reforms, or promises thereof, in several countries of Eastern Europe, but chiefly in the form of "position taking".

91. Even so, the volume of funds actually committed has remained comparatively small - perhaps $2.5 billion at the most in any one country. Total commitments to the East (omitting the former German Democratic Republic) at present amount to perhaps $8-10 billion. Furthermore, with the exception of some large deals in the electronics and automobile sectors, the value of each commitment, let alone disbursement, has remained rather small, and has actually tended to decrease as these economies have opened up. Not only that, disbursements have lagged far behind commitments, with several joint-venture agreements remaining no more than empty shells. The amounts disbursed are not known with any degree of precision, but recent estimates place them at one fourth to one fifth of total committed sums, perhaps $2.5 billion at most. In some cases, especially in Hungary and Poland, joint or foreign-owned ventures have been of the opportunistic kind, essentially rent-seeking and often unintentionally encouraging capital flight.

92. The potential for foreign direct investment in the reforming countries is considerable. Whether this will materialize, and when and how, are questions that cannot be answered without speculating on the reform course. Two factors need to be taken into account. One is that the reforming countries are competing for the excess savings managed mainly by the transnational corporations. These corporations' investment strategies are determined, by and large, by standard commercial considerations: expectations about the rate of return on capital (especially with a fairly short-term horizon), taking into account the repatriation of profits, and the uncertainty around that expected yield. Although for reforming countries the expected yield may rival that on investments, say, in the newly industrialized economies, at the present time the uncertainty of that return tends to be considerably larger than that in many traditional host countries.

93. For as long as uncertainty about the economics and politics of reforms in the East remains as large as it has recently been, foreign investors might continue exploring business opportunities, but they are unlikely to commit themselves full-scale to moving production facilities en masse into these countries. That may happen in the future, once economic stability is restored, basic infrastructure (such as telecommunications, roads, commercial banking and property rights) is firmly in place and other obstacles to the transition begin to be overcome.

94. Even if the economic transformation were to result in the East's quickly improving its absorptive capacity, the total amount of foreign capital that might flow into the region would probably not entail major diversions from potential foreign direct investment into developing countries. For one thing, the vast bulk of developing countries have not really seen any substantial inflows of the private direct and portfolio investment in recent years. Perhaps more important is the fact that if investors perceive that good opportunities exist, either in developing countries or in countries in the East, there is every reason to believe they will be able to muster sufficient funds.

95. The financing of the East's transition will create a greater demand for the world's savings than would have occurred if the East had not undertaken its revolution. Previously, private firms would have been very reluctant to invest there, and the question of assistance from the developed market economies would not have arisen. Germany would not have had to face the question of financing the reconstruction of the former German Democratic Republic, and helping it to approach its own standard of living. These new demands for capital can be expected to create an upward pressure on interest rates which will affect all countries, especially the most heavily indebted countries.

## IV. DEVELOPMENT ASSISTANCE PROVIDED BY THE EAST

96. One of the most immediate effects of the changes in Europe has been on the development assistance provided by Eastern Europe and the Soviet Union. This assistance was primarily motivated by socialist solidarity and international commitments which no longer have the same force. For ideological and political reasons, these countries often opted for rather unconventional forms of assistance, channelling most aid to selected countries with a commitment to broad-based industrialization in the context of a sizeable State sector. This applied most notably to the other formerly planned economies, which benefited from the transferable-rouble trade and payments regimes.

97. The aid was tied two ways and usually concealed through various price concessions, because the donors defined their aid much more inclusively than is customary in OECD countries and provided most of it directly through net merchandise exports. Moreover, as a rule they refused to subscribe to international conventions on ODA. 22/

98. In cases where assistance took the form of merchandise trade, some of the disbursements can be tracked on a net basis by examining trade imbalances. If aggregated balances run consistently in one direction over a protracted period of time, some part of the gap may be financed by long-term capital transfers, possibly grants in aid. 23/ Inasmuch as such flows were routinely provided at concessionary interest rates (customarily between 2 and 4 per cent) with long grace and repayment periods, cumulative trade imbalances provide an indication of net transfers.

99. The cumulative trade imbalances of Eastern Europe and the Soviet Union combined with non-socialist developing countries expanded over time and reached $96.4 billion in 1989. The Soviet Union's cumulative surplus expanded from $0.2 billion in 1962 to $68.4 billion in 1989. Eastern Europe's trade balance started at $0.1 billion in 1960 and ended in 1989 with a cumulative surplus of $28.1 billion. With few exceptions in the mid-1970s, there was a fairly consistent rise in this surplus until the latter half of the 1980s. These overall surpluses, however, cannot easily be disaggregated among the various developing-country partners for lack of data.

100. Eastern Europe and the Soviet Union ran sizeable and growing cumulative imbalances with the three developing-country CMEA members. In 1960 this imbalance amounted to about $17 million and, by 1989, $36 billion. The real value of these transfers had, of course, eroded over the years as a result of upward price drift. But the data suggest none the less a substantial real increase in the cumulative volume of aid, especially from the Soviet Union (which accounted for 88 per cent of the total).

101. With respect to the eight CMEA cooperants, the cumulative surplus rose too, particularly since the mid-1970s, when the first such agreements were signed. This was especially so for the Soviet Union. The Soviet share of the surplus accounted for around 57 per cent of the total surplus in 1989. For the third group of developing countries defined earlier - those with "close ties" with CMEA - there was also a sizable rise in the cumulative surplus, particularly Eastern Europe's. But its total value, by and large, stagnated at the 1980 level.

102. Statistics on aid levels that the Soviet Union and three Eastern European countries (Bulgaria, Czechoslovakia and the German Democratic Republic) submitted during the 1980s to the United Nations, using as basis their definitions, showed development assistance approximately at or better than the international target of 0.7 per cent of GDP set for the Second United Nations Development Decade declared for the 1970s; these proportions on the whole rose slightly over time.

103. OECD also attempted to measure, according to its definitions, aid extended by Eastern Europe and the Soviet Union. What stands out from their figures is that the share of multilateral assistance provided by the East remained negligible - below 1 per cent of the estimated total - and that there was an appreciable decline in the nominal value of assistance provided from 1987 on. In addition, traditionally, the vast bulk of assistance has been extended by the Soviet Union. Also, the major share of the increment in ODA provided in the second half of the 1980s was from the Soviet Union, which in 1989 extended 90 per cent of the total of assistance.

104. The vast bulk of assistance was earmarked for other planned economies, in the first instance the three developing-country CMEA members. In 1988, the shares of these and other developing-country planned economies were about 73 and 13 per cent, respectively.

105. The percentage of disbursements to GDP as estimated by OECD - between 0.14 in 1975 and 0.23 per cent in 1985 - amounts to only about one fifth to one fourth of the levels that the donors among the European planned economies claimed for themselves. If OECD's estimates for the East are augmented with estimates of the non-conventional forms of resource transfers for development purposes, such as price concessions, the overall assistance record of the former planned economies of Europe can be situated above the average of DAC members.

106. As part of their closer integration into the global economy, the countries of the East can be expected, in the future, to become aid donors in the DAC context, joining with the OECD countries in multilateral aid. However, the provision of such ODA will come gradually and will very largely depend on the success of the transition process.

107. At the present time, aid to former political allies is being drastically reduced or abandoned altogether. Furthermore, the substantial economic assistance embedded in and transmitted through the transferable-rouble trade and payments regimes has all but disappeared. Also, the fairly easy access to scientific and technical assistance from the East and temporary employment no longer exists or will soon be reduced to minimal levels. Especially Cambodia, Cuba and Viet Nam, but also Afghanistan, Angola, Ethiopia and Mozambique, will in the end have to come to grips with sharply declining real levels of development assistance from the East. The more painful the transition in terms of socio-political imbalances, or even only in terms of the length and depth of the recession in the East, the greater its impact will be on these selected developing countries.

108. In view of their economic difficulties, the countries of Eastern Europe and the Soviet Union are also taking steps to obtain the repayment of the debt they are owed by developing countries as quickly as possible, even though this might be at a large discount.

109. The former German Democratic Republic concentrated its aid on technical assistance in the form of professional training in the country's educational institutes or in special schools. It also provided training on the job. Whereas Germany's aid policy will have no socialist orientation, the reunified State might wish to capitalize on the good relations that the former German Democratic Republic established with a number of countries, particularly in sub-Saharan Africa, which had few relations with the Federal Republic of Germany. 24/

110. Because of the emerging labour shortages in the late 1970s, and as a way of meeting development-assistance commitments, including technical and scientific training, and to enable developing countries to begin servicing their long-term debt, arrangements were made for citizens, mainly from the three developing-country CMEA members, to be gainfully employed in Eastern Europe or the Soviet Union. The exact numbers are not known. However, the largest contingent of migrant workers came from Viet Nam - perhaps half a million at its peak. This is another form of assistance that is rapidly coming to an end.

## V. MIGRATION FROM THE EAST

111. Until late 1989, labour migration from Eastern Europe and the Soviet Union was not encouraged. The exceptions were Hungary and Yugoslavia, which had allowed their citizens to work abroad on whatever terms were available. The exact numbers are not known. In the case of Hungary, the numbers, by

1989, may have been several tens of thousands at most. In the case of Yugoslavia, however, hundreds of thousands of migrants had moved to Western and Northern Europe in search of better opportunities as early as the 1960s.

112. Particularly as a result of the Helsinki process, travel restrictions had been eased in many of the countries of Eastern Europe, and many of their citizens had visited other countries, especially in Western Europe and North America. One of the most glaring exceptions was the German Democratic Republic. However, in 1989, Hungary, in dismantling the wired fences that ran through its territory, allowed East Germans to cross into Austria, and thereby set in motion a massive migration from the German Democratic Republic into the Federal Republic of Germany that brought about the opening of all the borders of the German Democratic Republic and the collapse of one-party rule in the face of the obvious demonstration that the regime lacked sufficient popular legitimacy.

113. The principle that there were two halves of Europe with very little interconnections, and that a State could withhold from its citizens the right to travel, was breached in a matter of months. The long-term consequences of much greater mobility in the whole continent of Europe could be enormous. Much will depend on whether the countries in transition will be able to recover their economic dynamism and enable their citizens to enjoy stability and rising living standards. Continuous economic decline and ethnic strife could trigger off waves of migration on an unprecedented scale, which could strain relations between the local population and the new migrants, and strain relations between the different European countries.

## VI. PROBLEMS ENCOUNTERED IN ECONOMIC REFORM

114. Democracy and the promotion of rights of individuals have been seen as ends in themselves by the citizens of the countries of Eastern Europe. More participatory democracy may also be a necessary precondition in Eastern Europe and the Soviet Union for making the inevitable social costs of macroeconomic stabilization and structural change socially acceptable. 25/ However, the task of building up a consensus in society that would enable the Government's policies to be effectively implemented is considerably complicated by the rapid economic deterioration in many of the countries, resulting in sharp contractions in output and domestic demand, rising unemployment, often accelerating inflation or stubbornly high inflationary pressures, substantial volumes of capacity idled through lack of inputs or demand, and very slow supply responses. For the Governments of the East to create viable and vibrant democratic institutions in a short period of time would itself be a Herculean task. Yet, at the same time, they have, as it were, the task of cleansing the Augean stables - the economic and environmental devastation left by decades of neglect.

115. The very dismantling, after at least forty years of detailed administrative management, poses particular problems and encounters several obstacles. In some countries, they include a lack of familiarity with how

markets really operate; the absence of the institutions, legal bases and financial infrastructure of the market economy; and the need to erect a macroeconomic coordination mechanism to take the place of central planning. Another problem has been the frustration of the expectations of individuals that the reforms would on the whole preserve most of the benefits that they had been taking for granted under administrative planning.

116. Even when a clear decision for moving toward marketization exists, putting in place the market economy involves the task of what needs to be done, how quickly the various components can be taken up, and in what order that should be done. The essential features of a market economy range from the technical instruments of intermediating in a market environment, such as normally conducted through a commercial-banking infrastructure, to the legal instruments that are the very foundation of a pluralistic society, such as civil and commercial codes.

117. The solution of deeply rooted structural problems will take time, commitment and forbearance on the part of the local populations. It will also lay claim to considerable outside assistance, financial, as well as other forms of aid, to alleviate the adjustment burden and anchor market orientation more firmly as soon as possible, and also to carry the process through at as steady a pace as feasible.

118. One issue that cannot be avoided in the transition towards the market economy is that of privatization. In Eastern Europe something like 80 per cent of the economies were State-controlled and their Governments see that there is no possibility of creating a private enterprise economy without the disciplines that come from private ownership of industry. The Soviet Union is different from its neighbours in that it has not yet made such a firm decision to move towards privatization. Privatization does raise many issues about property rights and equity. The Eastern countries do not have the capital markets and the amounts of savings in relation to the assets that are to be sold as exist in developed market economies. Moreover, much of Eastern Europe's industry is operating at a loss, is probably unsaleable on international markets and would at present find very few buyers domestically. Although the different privatization schemes being adopted do, then, involve the free distribution of assets, they do not involve a vast redistribution of income-earning assets. In future, though, the privatized industries, many of them drastically slimmed down, should be income-generating.

119. Estimates of the time taken to privatize State enterprises vary, but it is difficult to believe that the progress will be as slow as privatization schemes in the developed market economies. The economic difficulties in the East and the urgency of putting in place a functioning market economy are simply too great to allow for measured progress.

120. The success of privatization and, more generally, private enterprise depends, to a great extent, on investment in infrastructure, which is largely a government responsibility. For lenders to view lending to the public sector as in conflict with that to the private sector, and to set arbitrary limits on

the absolute or relative amounts lent to either sector would imply a lack of pragmatism.

## VII. CHANGES IN EAST-WEST RELATIONS

121. In 1989, the ideological struggle that had rendered international cooperation difficult was, in effect, over. Swept aside was the view that the world was split into two mutually antagonistic camps between which war, if not inevitable, was at least likely if efforts to secure the peace were not made. The help extended by citizens of Austria, Czechoslovakia, the Federal Republic of Germany, Hungary and Poland to enable the citizens of the then German Democratic Republic to reach freedom in the Federal Republic showed that the common values of these European countries were far greater than any ideological differences that their Governments had, and that indeed the natural relationship between them was one of friendship.

122. The role of Governments in the East in the ending of the cold war should not be overlooked. In particular, it was the Soviet Government that announced unilateral disarmament measures in 1988, stating that it was adopting an openly defensive military doctrine, and in 1989 made it clear that it would not intervene to affect the course of events in Eastern Europe. These events in themselves affected the entire security position for the developed market economies, and in particular the countries of the North Atlantic Treaty Organization (NATO), which, for over 40 years, had insisted that they had to invest in defence, maintain overseas military installations and provide military assistance to different countries in order to deter the threat from the East. It is impossible to calculate how much would have been spent on defence in the absence of the cold war, and how much will be saved in future with its end, which, as stated above, was largely brought about by actions by Eastern Governments; but the sums must be greater than any likely expenditures to be incurred on assistance to the East. 26/

123. It is important to note the very strong commitment towards helping Eastern Europe, after its abandonment of one-party rule, that the developed market economies have made. This can be contrasted with the commitment towards developing countries. It can be argued that the developed market economies rarely had a comparable commitment towards the developing countries. If these countries were to decay economically, this was not taken to mean a failure of their own socio-economic system nor to necessarily call for exceptional assistance: in this sense, the developing countries were left to chart their own future.

124. Failure in Eastern Europe would hardly be tolerable for the developed market economies, particularly after the enormous costs associated with the cold war and the claims made for the superiority of the market system over the command economy system. For this reason, assistance to Eastern Europe will take a special place in their list of priorities, and the plight of the people of Eastern Europe will evoke a special response.

125. If such assistance is successful, the results in terms of global cooperation could be very great. If it is unsuccessful, the consequences could be catastrophic and call into question the very wisdom of assisting countries towards greater integration in the global economy, and asking them to make rapid progress towards new forms of government and economic system. In a fundamental sense, then, the most important thing for the developing countries and for global cooperation is that the reform process in the East be a success and that the assistance extended to ensure its success be effective. To contrast assistance to the East with assistance to developing countries and to imply that the former is being extended at the cost of the latter could well be an over-simplification and might constitute a misreading of history. If the Eastern countries were to fail, there would be no beneficiaries, and certainly not the developing countries. If they were to succeed this could have profound consequences for global cooperation and go a long way to overcoming "aid fatigue".

126. The course of events in Germany provided a stark illustration of the consequences of a sudden opening of the borders between countries with very different real incomes. Any serious deterioration in the economic situation in the East that would give rise to massive demographic movements, would probably elicit considerable assistance, especially from Western Europe. This would occur at a time that overall national budgets were under downward pressure. Although there is little prospect that assistance budgets will be raised any time soon, any sizeable calamity arising in the East, or in the developing world for that matter, would probably persuade the electorate of the wealthier countries of the appropriateness of mustering additional resources for the causes at hand. But this possibility is more likely when buoyant growth in donor countries can be secured, something that is not at all certain at this stage.

127. On the other hand, one of the first beneficial effects of the end of the cold war is already being seen in planned reductions in military spending. In discussions of the availability of resources to assist the transition, particularly in the medium to long run, the beneficial effect of a sharp reduction in military budgets and ancillary expenses is often overlooked. As mentioned above, for a long time these expenditures were justified by the cold war. The dissolution of the Warsaw Treaty Organization as a military alliance in March 1991 shows that the security picture has changed completely. Whereas the peace dividend resulting from converting military facilities to civilian uses, while not completely superfluous, is generally small, the savings in terms of expenditures that would have been earmarked for military purposes could in time be very substantial. Such a reduction in expenditures will in the first instance be deflationary, especially in countries where it will be utilized to improve the budget balance. None the less, lower military expenditures can lead to lower taxes or less crowding out in financial markets, which cannot but be beneficial. Lower military expenditures and diminished tensions may furthermore strengthen the environment for regular commercial interchange between countries that used to belong to differing social and economic systems.

128. The movement towards pluralistic decision-making and marketization in the East together call for rapid integration of the reforming countries into all aspects of the global economic framework. With the opening of the East and the more active participation in all forms of international economic relations, management of the global economy through the instruments already in place could be facilitated. It might also create a sufficiently favourable atmosphere for reconfiguring key aspects of the global economic framework so as to attune its institutional features better to ongoing policy concerns. Many developing countries would stand to benefit from this.

129. One of the key items in the emerging European cooperation is combating environmental degradation, that is, by trying to clean up the heavily polluted environment in parts of the East and assisting the restructuring process with up-to-date technology and environmentally friendlier production processes. This requires not only technical advisory services, but also substantial capital to finance imports of the necessary equipment.

130. The reforming countries have also regularized their position in international economic organizations. Thus all countries of Eastern Europe, except Albania, are now members of IMF and the World Bank; negotiations with Albania are currently taking place. Except Bulgaria, all countries of Eastern Europe are contracting parties in GATT. Negotiations about Bulgarian accession, first requested in 1986, have received a new impetus. Countries with an odd status in GATT (such as Czechoslovakia), or that entered through a strange arrangement (such as Poland and Romania) or never attained an unencumbered contracting-party status (such as Hungary) have by now regularized their position or are in the process of renegotiating their accession status. The Soviet Union acquired observer status in early 1990 and is eager to join GATT as a full contracting party.

131. At the time of the Group of Seven's Houston summit of July 1990, these countries showed considerable good will towards the Soviet Union's participation in IMF and the Bank. A Soviet delegation participated in last year's autumn meetings in Washington, an IMF mission was instrumental in preparing a report on the state of the Soviet economy for the Group of Seven, and for a while sufficient political support was garnered for creating a special "associate status" for the Soviet Union. This would have permitted the institutions to furnish technical assistance at several different levels, but not to dispense loans, and the Soviet Union to get acquainted with the workings of the organizations. The events in the Baltic States in early 1991 have put that plan temporarily on hold. Yet, it is still possible that the principles earlier worked out will be acted upon soon.

132. IMF and Bank membership raises the issue of the debt burden, which is very substantial for many countries of the East. As noted above, in the light of the exceptional treatment recently given to Poland, a resolution of the chronic debt problem of other transitional economies may be in the offing. Although the precedents of debt forgiveness for the East might reduce the room for manoeuvre of creditors in giving the same treatment to other debtor countries, as financial institutions cannot write off the vast bulk of debt,

the leniency shown towards Poland itself could presage similar advantages for debtor developing countries.

## VIII. EVENTS IN EASTERN EUROPE AND THE UNITED NATIONS SYSTEM

133. The reform process in the East has elicited enthusiastic commitments for assistance and cooperation, mostly but not exclusively from Western Europe. The Commission of the European Communities has been entrusted with the overall coordination of the financial assistance efforts of 24 industrial countries that have joined together in this enterprise. The IMF and the World Bank are supplying policy advice and financial resources.

134. But changing the institutions and policies in Eastern countries involves more than financial support. Statistical information has to be collected along different principles, social policies have to be revised without excessive social cost, and dire environmental problems have to be tackled.

135. In all these areas, the United Nations system has much to offer by way of technical advice and collective experience, and it is rightly and heavily charged by requests for aid and advice from Eastern countries. It has an obvious and important function in this process.

136. However, it is essential also to address the concerns of other actors in the world economy who fear that this effort on behalf of the reform process in the East must lead to a diversion of attention from the problems of developing countries. This is a genuine concern that will not be dispelled by statements that the negative effects for developing countries will at worst be modest. Everything suggests that the transition in the East will yield substantial gains for all in the long run, but it is essential to ensure that the poorest and most vulnerable parts of humanity are not adversely affected in the short to medium term. An enhanced global dialogue and very clear policies will be necessary to dispel the anxieties of developing countries that progress in the East will not be at their expense, but that they are engaged in a positive-sum game in which all have a stake in the progress of the others.

### Notes

1/ The term "East-West" largely reflects the division of Europe after the Second World War. As this ideological division affected almost all areas of the globe, it has no geographical meaning. "West" is a loose term referring in general to developed market economies, several of which - Australia, Japan and New Zealand - are not "West".

2/ The designation "East" is used as a shorthand to denote Albania, Eastern Europe, the Union of Soviet Socialist Republics and Yugoslavia. Eastern Europe is used here chiefly for presentational convenience to group together the smaller countries of the eastern part of Europe that used to be centrally planned. The core consists of Bulgaria, Czechoslovakia, the former

Notes (continued)

German Democratic Republic (until late 1990), Hungary, Poland and Romania. Although Albania (more recently) and Yugoslavia (from the very beginning) form part and parcel of the ongoing transformations, they are omitted from most of the empirical analyses here. Traditionally, Yugoslavia has not been included in "Eastern Europe" or "European planned economies", it having abandoned planning as early as the 1950s. Albania is omitted from most computations simply because the pertinent empirical information is not available.

3/ Until its formal dissolution in June 1991, CMEA had 10 active full members (Eastern Europe as defined and the Soviet Union, and Cuba, Mongolia and Viet Nam); one inactive full member (Albania); one associate member (Yugoslavia); nine cooperants (Finland and eight developing countries - Afghanistan, Angola, Ethiopia, Iraq, Mexico, Mozambique, Nicaragua and the former Democratic People's Republic of Yemen) and a number of ad hoc observers.

4/ With effect from 3 October 1990 the Federal Republic of Germany and the German Democratic Republic united to form one sovereign State under the designation "Germany".

5/ The term "transferable rouble" could be misleading as it was neither convertible nor even transferable. Most exchanges within the CMEA were bilateral; multilateral trade accounted in the past for 1 per cent of total CMEA trade at most.

6/ Figures from World Population Prospects, 1990 (United Nations publication, Sales No. E.91.XIII.4).

7/ For instance, in United States Arms Control and Disarmament Agency World Military Expenditures and Arms Transfers 1989 (Washington, D.C., 1990), the GNP of the Soviet Union in 1988 was put at $2,526 billion and that of the United States at $4,881 billion, a ratio 1:1.9.

8/ See, for instance, International Institute for Strategic Studies, The Military Balance 1990-1991, p. 33.

9/ Figures from International Monetary Fund, World Economic Outlook (May 1991), table B, p. 126.

10/ Data from United States Arms Control and Disarmament Agency, World Military Expenditures ... .

11/ A detailed examination with ample empirical detail, including a discussion of the problems faced because of inadequate official data, is provided in World Economic Survey, 1991 (United Nations publication, Sales No. E.91.II.C.1), chap. 6.

Notes (continued)

12/ By article XXIV, "Territorial Application - Frontier Traffic - Customs Unions and Free-Trade Areas" the contracting parties agreed, inter alia, that "the purpose of a customs union or of a free-trade should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other contracting parties with such territories". See General Agreement on Tariffs and Trade, Text of the General Agreement (Geneva, 1986), art. XXIV, para. 4. (Sales No. GATT/1986-4.)

13/ Finland was also a cooperant.

14/ New York Times, 10 May 1991.

15/ For a broad review of the various types and amounts of assistance, see Economic Survey of Europe, 1990-1991 (United Nations publication, Sales No. E.90.II.E.1), pp. 212-223; Economic Survey of Europe, 1990-1991 (United Nations publication, Sales No. E.91.II.E.1), pp. 112-118; and Economic Bulletin for Europe, vol. 42 (1990) (United Nations publication, Sales No. E.90.II.E.37), pp. 79-86.

16/ The IMF has also introduced two important extensions of the compensatory and contingency financing facility, to enable the reforming countries most affected by the run-up in oil prices to cover the larger-than-expected current-account deficits. The beneficiaries are Bulgaria, Czechoslovakia, Hungary and Poland.

17/ Article XIV is concerned with transitional arrangements.

18/ Washington Post, 28 April 1991.

19/ See Economic Bulletin for Europe. vol. 42 (1990), p. 83.

20/ Pologne/Hongrie: Assistance à la restructuration économique is the name of the Group of Twenty-four's programme for the East, now applicable to virtually all countries except the Soviet Union.

21/ For a broad review of the state of affairs until about 1988, see East-West Joint Ventures: Economic, Business, Financial and Legal Aspects (United Nations publication, Sales No. E.88.II.E.18).

22/ See Proceedings of the United Nations Conference on Trade and Development, Fourth Session, vol. I Reports and annexes (United Nations publication, Sales No. E.76.II.D.10) and "Joint statement of Group D and Mongolia regarding the launching of global negotiations" (A/38/479, 1983).

23/ Whereas earlier it was assumed that most loans from the East would be turned into grants, more recently the East has tried to have developing countries repay their debts. Thus far, only partial results have been achieved, chiefly by the debtor country shipping goods and thus generating an export surplus with the creditor country.

Notes (continued)

24/ Siegfried Schultz, "Features and trends of East Germany's aid and trade with the third world" in The USSR and Eastern Europe in the Global Economy, Marie Lavigne, ed. (Cambridge, Cambridge University Press, 1991 (forthcoming)).

25/ For a rounded analysis of the multiple problems of the transition in the eastern part of Europe, see Economic Survey of Europe, 1989-1990, pp. 5ff. and Economic Survey of Europe, 1990-1991, pp. 123-191.

26/ An indication of the resources consumed in the East-West strategic struggle is that in 1940, before its entry into the Second World War and before the onset of the cold war, the United States' expenditure on national defence was 1.7 per cent of GNP; and that, in the 1980s when a military build-up was under way precisely to counter the threat perceived to emanate from the Soviet Union, it reached a maximum, in 1986, of 6.7 per cent. Clearly, not all the increase can be attributed to the cold war, but the difference - five percentage points of GNP - provides some indication of the cost to the United States of its global commitments. It could be added that the neutral European developed market economies - Austria, Finland, Ireland, Sweden and Switzerland - had defence burdens from 1 to 3 per cent of GNP.

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